



The City of London Law Society

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Response to Building Societies (Funding) and Mutual Societies (Transfers) Act 2007 consultation paper – September 2008

The City of London Law Society (CLLS) represents over 13,000 City lawyers, through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi-jurisdictional legal issues.

The CLLS responds to a variety of consultations on issues of importance to its members through its 17 specialist committees. This response to the Building Societies (Funding) and Mutual Societies (Transfers) Act 2007 consultation paper – September 2008 forms has been prepared by the CLLS Regulatory Law Committee. Members of the Regulatory Law Committee advise a wide range of firms in the financial markets including banks, brokers, investment advisors, investment managers, custodians, private equity and other specialist fund managers as well as market infrastructure providers such as the operators of trading, clearing and settlement systems.

We are writing to respond on two aspects of the consultation paper: the proposal to allow HM Treasury the power to increase building societies' wholesale funding limits to 75% of their funds and the proposed change to the priority order on winding-up. The Committee is concerned by the proposal to increase wholesale funding limits and would ask HM Treasury, in the strongest terms, to reconsider and revisit this proposal for the reasons set out below.

Increase in wholesale funding limits

The proposal seeks to grant HM Treasury the power to increase wholesale funding limits on building societies from 50% to 75% of their funds. This appears to be an unnecessary increase as the current figures show that in 2007, despite a maximum of 50% being available, building societies only sought funding of 31.2% of their funds by wholesale funding. This suggests, not only that building societies do not actually require such substantial amounts of wholesale funding, but that they are choosing to approach wholesale funding in a prudent manner.

Increasing the limit to 75% represents a substantial increase from the 50% limit currently available and would be an extremely large increase in respect of the amount which was actually used by building societies last year. As the Government notes that it is not aware of any building society which would want to make use of a limit higher than 50%, this seems an unnecessary amendment. We note that once the limit is raised it cannot be reduced.

We understand that the Treasury does not intend to make changes to the limits immediately but is seeking this amendment to allow itself the power to increase the limit at a future date, to encourage building societies to have greater flexibility over their funding strategies and to allow them to compete more equally with banks. Nevertheless, the Committee feels strongly that in the current difficult economic and banking climate this would be an unnecessary and imprudent amendment to make. Mervyn King in his speech to the CBI on 21 October 2008 underlined that *banks* had been too dependent on credit from wholesale sources and this had some part to play in the difficulties banks are now facing. Given the nature of wholesale funding currently, offering building societies this flexibility could come at the price of their stability. Making it possible for building societies to increase their dependence on riskier forms of funding such as wholesale funding should not be encouraged especially when recent events have shown that business models which are heavily dependent on wholesale market funding can give rise to considerable risk to depositors and taxpayers.

Winding-up priority

HM Treasury seeks to safeguard the rights of members of building societies in relation to the proposed increase of wholesale funding limits, by changing the order of priority on insolvency, so that the liabilities of creditors will not take priority to those of shareholding members. The Committee supports this and feels strongly that members should not rank behind creditors on insolvency. However this 'safeguard' to protect members should not depend on the pre-existence of the proposed increase in wholesale funding limits.

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